No. 47494-8-II

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

MUTUAL OF ENUMCLAW INSURANCE COMPANY,

Appellant/Cross Respondent,

v.

MYONG SUK DAY, dba STOP IN GROCERY,

Respondent/Cross-Appellant.

APPEAL FROM THE SUPERIOR COURT
FOR PIERCE COUNTY
THE HONORABLE STANLEY J. RUMBAUGH

REPLY BRIEF OF RESPONDENT/CROSS-APPELLANT

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I. REPLY ARGUMENT

If this Court agrees that the judgment based on the jury's verdict should be affirmed, there is no reason to decide this cross-appeal. Although the issues on cross-appeal are relevant only if this Court would otherwise reverse and remand for a new trial, MOE's response nevertheless demonstrates that MOE seeks to divert this Court's attention from the real issues on review.

A. MOE is bound as a matter of law to the consent judgment.

1. An appeal from final judgment brings up a partial summary judgment that prejudicially affected it.

As MOE points out (MOE Rep. 45 n. 22), the Order denying partial summary judgment is not at CP 314. It is at CP 594-96. The order is attached as an Appendix to this brief. We apologize for this citation error. But it is not dispositive.

Contrary to MOE's claim (MOE Rep. 45), the trial court did not address this issue as an evidentiary motion in limine. Instead, the trial court in the order challenged on cross-appeal denied Day's motion for partial summary judgment establishing a presumption of harm and coverage by estoppel, on the grounds Day "has not yet established that Mutual of Enumclaw acted in bad faith." (CP 595-96)

The jury, of course, did find that MOE acted in bad faith. (CP 1765) The trial court should have resolved the legal consequences of the jury's determination that MOE had acted in bad faith on summary judgment, and the trial court's denial of summary judgment can be reviewed on appeal from the final judgment. *Kaplan v. Nw. Mut. Life Ins. Co.*, 115 Wn. App. 791, 799, 65 P.3d 16 (2003) (denial of summary judgment reviewable on appeal from final judgment after trial where "the decision on summary judgment turned solely on a substantive issue of law") (citation omitted), *rev. denied*, 151 Wn.2d 1037 (2004). Contrary to MOE's argument that Day is not "permitted" to appeal the denial of partial summary judgment (MOE Rep. 45), an appeal (or cross-appeal) of a final judgment brings up for review any ruling prejudicially affecting the decision designated in the notice, RAP 2.4(b), as the court recognized in rejecting a party's claim that review was limited by RAP 5.3(a)(3) in *Gomez v. Sauerwein*, 172 Wn. App. 370, 289 P.3d 755 (2012) (MOE Rep. 45), *aff'd* 180 Wn.2d 610, 331 P.3d 19 (2014).

Given MOE's arguments for reversal on appeal, review of the trial court's summary judgment is necessary to define the scope of any remand. Once the jury decided that MOE had acted in bad

faith, coverage by estoppel for the reasonable amount of Day's settlement and the presumption of harm (on which the jury was in any event not instructed; *see* Day Resp. 37-38) follows as a matter of law. *Miller v. Kenny*, 180 Wn. App. 772, 798-99, ¶¶51-52, 325 P.3d 278 (2014); *Besel v. Viking Ins. Co. of Wisconsin*, 146 Wn.2d 730, 738, 49 P.3d 887 (2002) ("the amount of a covenant judgment is the presumptive measure of an insured's harm caused by an insurer's tortious bad faith if the covenant judgment is reasonable under the *Chaussee* criteria"). Therefore, if this case is remanded for any reason, this Court should address the trial court's erroneous denial of summary judgment on this issue of law.

2. On any remand, the jury's finding of bad faith binds MOE to the consent judgment.

Although MOE expends considerable effort in its reply arguing that the jury's findings of emotional distress damages caused by MOE's bad faith is insufficient to bind it to the "floor" of damages measured by the reasonable consent judgment Day reached with the injured plaintiffs, MOE does not respond substantively to the consequence of the jury's finding of bad faith. In particular, MOE does not address the holding of *Mut. of Enumclaw Ins. Co. v. Dan Paulson Constr., Inc.*, 161 Wn.2d 903, 922, 169 P.3d 1 (2007) (Day Resp. 47), which held *as a matter of*

law that because MOE's bad faith conduct "caused significant uncertainty and increased risk" to its insured in that case, MOE was liable for a negotiated settlement reached after MOE tried to engage in *ex parte* contact with the arbitrator in an effort to bolster its position in its coverage dispute with the insured.

MOE's conduct here was far more egregious than that at issue in *Dan Paulson,* and the uncertainty and risk MOE caused its insured Day was much more predictable and certain to be the consequence of its bad faith. Rather than merely attempt to use the underlying lawsuit to bolster its claim against coverage, MOE affirmatively misled its insured Day, and the injured plaintiffs, about the true nature of the coverage dispute. As a result, Day was forced to consent to entry of a judgment exceeding $7.9 million in a reasonable settlement that could have and should have been avoided entirely had MOE owned up to its responsibility to provide full coverage to Day based upon the actions of its agent. As previously argued (Day Resp. 31-34), "even though the agreement insulates the insured from liability, it still . . . constitutes a real harm because of the potential effect on the insured's credit rating . . . damage to reputation and loss of business opportunities."

Safeco Ins. Co. of Am. v. Butler, 118 Wn.2d 383, 399, 823 P.2d 499 (1992) (quoted case omitted).

Day suffered harm as a matter of law under *Dan Paulson*. To the extent necessary to ensure that on remand MOE faces the established legal consequences that flow from a finding that an insurer breached its duties of good faith under *Tank v. State Farm Fire & Cas. Co.*, 105 Wn.2d 381, 715 P.2d 1133 (1986), this Court should rule that the trial court erred in failing to grant summary judgment on this issue of law.

B. Day is entitled to reformation of the insurance contract based on her mistake as to coverage, fostered by MOE's inequitable conduct.

1. Day argued below that her mistaken belief she had liquor liability coverage was grounds for reformation, and in any event the trial court should use the correct test on any remand.

Day did not invite the trial court's error in failing to recognize grounds for reformation in this insurance contract. Although discussed by both parties in terms of mutual mistake, Day clearly relied below on the *insured's* mistake in believing she had coverage as grounds for reformation, arguing that reformation should be granted "even with no agreement there was a mistake and even with highly disputed facts." (CP 1828; *see also* 2/9/15 RP 38 argument on reformation claim: "And so the question of mutual

mistake is answered completely by whether she would have requested it, whether she did request it at that time.")

Regardless whether the issue was preserved, this Court should decide the cross-appeal to set out the correct test for reformation of the insurance contract if remand is necessary. Principles of issue preservation are intended to foster the "efficient use of judicial resources . . . . by ensuring that the trial court has the opportunity to correct any errors, thereby avoiding unnecessary appeals." *State v. Robinson,* 171 Wn.2d 292, 304–05, ¶22, 253 P.3d 84 (2011). Here, the policy of avoiding "unnecessary appeals" supports consideration of this issue, which is not raised as grounds for a new trial, but on a conditional cross-appeal in order to ensure that the trial court correctly applies the law in the event of a remand.

2. An insurance contract should be reformed based on the insured's reasonable expectation of coverage.

MOE wrongly persists in an analysis of the parties' "mistake" that ignores the heightened duties both it and its agent Huh had to Day as an insured. Day's mistake was believing that she had the coverage her seller had a mistake that should have supported reformation regardless of Huh's intentions, particularly given the

trial court's rejection of Huh's denial of Day's request for coverage as not credible. (CP 2378-79) That MOE refused to admit to its agent's mistake is not grounds for denying reformation.

Moreover, there was clear and convincing evidence that Huh intended to provide Day the liquor liability coverage that her seller had even if the trial court had a basis to reject Day's testimony standing alone as insufficient. MOE cannot explain away the singular oddity that liquor liability coverage was the *only* liability coverage carried by Day's seller that was not continued in Day's policy MOE either maintained or increased every other coverage. (*Compare* Ex. 27 at 6, *with* Ex. 30 at 3) MOE further ignores the other evidence that Huh initially intended to provide Day liquor liability coverage, including that Huh told Day she was covered when Day first notified him of the claim, and that Huh did not raise the coverage issue when MOE's underwriting department called him in 2009 about the policy. (11/19 RP 136-37; 11/20 RP 132-33; Ex. 51)

This evidence substantially undermines MOE's argument that the policy could not have been reformed because "the parties' intentions were [not] identical at the time of the transaction." (MOE Rep. 48, quoting *Denaxas v. Sandstone Court of Bellevue, L.L.* C., 148 Wn.2d 654, 669, 63 P.3d 125 (2003)). To the contrary,

the trial court's findings here were that Day and MOE's agent Huh did in fact have "identical intentions" when Day told Huh she wanted liquor liability coverage and Huh agreed to obtain it for her. (CP 2378-81) MOE's attempt to distinguish the cases relied on by Day on the basis that the parties did not have "identical intentions" is misplaced.

In *Denaxas,* for instance, the parties had "identical intentions" because they had "identical information" concerning the size of the property to be transferred pursuant to their purchase and sale agreement. 148 Wn.2d at 668-69. Here, the parties did not have "identical information" – as the trial court found (CP 2379), Day thought she was obtaining liquor liability coverage, while MOE knew she had not. Consistent with the principle that the "tie goes to the insured," as MOE's own witnesses acknowledged in their testimony (11/19 RP 114; 11/24 RP 139; 11/25 RP 33), Day's mistaken belief that she was obtaining liquor liability coverage supported reformation of the contract.

MOE's response to Day's argument for reformation utterly ignores the quasi-fiduciary nature of its relationship with its insured, perpetuating its cavalier exaltation of its own interests in avoiding its duties to indemnify covered claims over the

expectations and interests of its insured. The doctrine of reformation on the basis of mistake based upon the inequitable conduct of the non-mistaken party is well-established. *See Cavanaugh v. Brewington,* 3 Wn. App. 757, 758, 477 P.2d 644 (1970) ("It is clear that reformation may be granted upon the unilateral mistake of one party accompanied by inequitable conduct on the part of the other"). Huh's belated denial of any intent on the part of Day to obtain the liquor liability coverage her seller had, combined with MOE's misconduct in accepting Huh's denial without any investigation or disclosure to Day, more than meets the standard of inequitable conduct. If this Court remands, it should direct the trial court to reform the policy in accord with the applicable law and with the parties' true relationship in mind.

Dated this 1st day of June, 2016.

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DECLARATION OF SERVICE

The undersigned declares under penalty of perjury, under the laws of the State of Washington, that the following is true and correct:

That on June 1, 2016, I arranged for service of the foregoing Reply Brief of Respondent/Cross-Appellant, to the court and to the parties to this action as follows:

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DATED at Seattle, Washington this 1st day of June, 2016.

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Reply Brief of Respondent/Cross-Appellant

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